January 10, 2022(Revised)

Small Industries Development Bank of India: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Bonds Programme	5,000.00	5,000.00	[ICRA]AAA(Stable); reaffirmed
Total	**5,000.00**	**5,000.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating for Small Industries Development Bank of India (SIDBI) factors in its position as an apex financial institution (FI) for the promotion and development of the micro, small and medium enterprises (MSME) sector in India. SIDBI was established under an Act of Parliament in 1990 and is jointly owned by the Government of India (GoI; 15.4% as on September 30, 2021), public sector banks (PSBs), insurance companies and other financial institutions (FIs).

To enhance SIDBI's competitive funding position, the GoI facilitates access to low-cost micro & small enterprise (MSE) funds[1] for onward refinancing to eligible lending institutions at competitive rates. The allocation for FY2022 was Rs. 55,000 crore at a concessional interest rate (Rs. 40,000 crore in FY2021). MSE funds accounted for 76% of SIDBI's total borrowings as on September 30, 2021 (73% as on March 31, 2021; 64% as on March 31, 2020). This supports the competitive cost of funds for the entity.

As a part of its lending operations and refinancing activities, SIDBI takes exposure to scheduled commercial banks (SCBs), private entities other than banks, and non-banking financial companies (NBFCs). In addition to a few exposures to NBFCs that turned non-performing this fiscal, some of the counterparties, especially in the direct lending segment (~8% of advances as on September 30, 2021), could be weak. However, SIDBI has largely provided for these exposures with it net non-performing advances (NNPAs) at a low level of 0.13% as on September 30, 2021 (0.12% as on March 31, 2021).

SIDBI's leverage[2] level stood at 6.57 times as on September 30, 2021 (7.91 times as on March 31, 2021), which is well within the regulatory permissible level. However, with the targeted credit growth, its borrowings are likely to increase but the leverage is expected to be ~8.5-8.7 times by March 31, 2022. SIDBI's capitalisation levels remain comfortable with a CRAR of 30.94% as on September 30, 2021 (27.49% as on March 31, 2021). This, in turn, is supported by lower risk weights of 20% to refinance the exposure of banks. SIDBI has a superior liquidity profile with positive asset-liabili ty gaps in the short as well as long term, which are supported by the matching tenure of the assets (refinancing loan book) and the liabilities (MSE funds). The liquidity profile is further supported by standby lines from banks, including the pending drawdown against the allocated MSE fund.

ICRA expects that SIDBI will continue to benefit from its role of an apex FI in the MSME development sector and its strategic importance to the GoI, driving the Stable outlook on the rating. Given the cap on lending margins, the earnings profile in terms of return on assets/equity (RoA/RoE) is likely to remain modest, though the profitability is likely to be sufficient for achieving the targeted growth without fresh equity capital requirements in the near to medium term.

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[1] *MSE fund is created out of deposits from SCBs against their shortfall in priority sector lending (PSL) targets*

[2] *Leverage = Total debt/Net owned funds; as per Reserve Bank of India (RBI) regulations, All India Financial Institutions (AIFIs) have to maintain a leverage of 10 times, though SIDBI received approval for a higher leverage of 12 times till July 31, 2022*

Key rating drivers and their description

Credit strengths

Strategic importance to GoI for development of MSME sector – SIDBI is an FI established in 1990 under an Act of Parliament (SIDBI Act, 1989). Under the Act, SIDBI has been described as a development bank established as 'the principal financial institution for the promotion, financing and development of industry in the small-scale sector and to coordinate the functions of the institutions engaged in the promotion, financing or developing of industry in the small-scale sector and for matters connected therewith or incidental thereto'. Currently, State Bank of India (SBI) is the largest shareholder with a stake of 16.73%, followed by the GoI at 15.40% and Life Insurance Corporation of India (LIC) at 14.25%. Other PSBs and institutions own the remaining share in the entity as on September 30, 2021.

ICRA, however, notes that in the absence of a single dominant shareholder or promoter, future capital raising, if any, will remain dependent on the ability and willingness of all the shareholders to contribute capital in a timely manner. Nevertheless, given the current capitalisation levels, the requirement for capital support remains limited in the near to medium term.

Capitalisation metrics remain strong – With the refinance business dominating SIDBI's loan book, the RBI has allowed it to borrow up to a leverage of 12 times till July 31, 2022 to meet the increasing refinancing requirements vis-à-vis the leverage of 10 times that FIs like SIDBI are allowed as per RBI regulations. Against this, SIDBI's leverage stood at 6.57 times as on September 30, 2021 (7.91 times as on March 31, 2020). SIDBI has exposure to various banks, which attracts a low-risk weight of 20%, resulting in strong capital adequacy levels with a CRAR of 27.49% (entirely Tier I) as on March 31, 2021 (26.62% as on March 31, 2020). The CRAR improved further to 30.94% as on September 30, 2021. ICRA notes that even with the change in the method of computing risk-weighted assets (for aligning with Basel III), the capital metrics will remain strong.

Strong asset quality indicators – SIDBI's overall asset quality is supported by low NPAs in the refinance book, which accounted for 82% of its lending portfolio as on September 30, 2021 (84% as on March 31, 2021). SIDBI witnessed slippages from its NBFC exposures in H1 FY2022. However, it has made full provisions on such exposures with gross NPA (GNPA) and NNPA ratios of 0.20% and 0.13%, respectively, as on September 30, 2021 (0.18% and 0.12%, respectively, as on March 31, 2021). The total exposures to NBFCs is estimated at 8.85% of the loan book as on September 30, 2021. Further, given the induced stress in the NBFC sector, the asset quality of some of these exposures could be monitorable, though these are expected to be limited in relation to the entity's operating profit and net worth.

Funding profile remains strong with MSE fund allocations – SIDBI's funding profile remains dominated by low-cost MSE fund/Rural Infrastructure Development Fund (RIDF) allocations. It has access to these low-cost funds, which are made available by banks against their shortfalls in meeting their PSL targets. The total borrowings under the MSE fund programme remain high at Rs. 1.08 lakh crore and comprised 76% of its overall borrowings as on September 30, 2021. Given its quasi-sovereign status, SIDBI mobilises funds at competitive rates from the capital markets in the form of bonds, commercial papers and certificates of deposit.

MSE/RIDF allocation for FY2022 was higher at Rs. 55,000 crore compared to Rs. 40,000 crore each for FY2021 and FY2020. Out of the total allocation of Rs. 65,000 crore for FY2022, Rs. 55,000 crore was towards MSE refinancing, Rs. 5,000 crore towards refinance in credit-deficient districts and the balance (Rs. 5,000 crore) towards the Cluster Development Fund. Continued allocations under MSE funds will remain important for SIDBI for maintaining a competitive cost of funds as well as the scale of its refinancing business and hence its profitability.

Credit challenges

Growth linked with availability of low-cost MSE fund allocations/RIDF deposits and refinance demand – SIDBI's growth prospects remain linked to the extent of coverage achieved by SCBs in meeting their PSL targets. As SCBs progressively achieve higher PSL targets, the overall allocation under MSE funds could drop, thereby affecting the growth prospects in the long term. Moreover, the MSE fund allocation of Rs. 1.83 lakh crore for FY2018-22 has, to a major extent, supported SIDBI's overall growth. Additionally, PSL shortfalls are allocated to other eligible AIFIs like National Housing Bank (NHB) and National Bank for Agriculture and Rural Development (NABARD) apart from Micro Units Development & Refinance Agency Ltd. (MUDRA). The annual allocation to SIDBI will also remain dependent on its relative importance compared to other AIFIs, which could result in lower allocations in case of increased allocation or preference to others.

Further, the demand for refinance from banks could remain muted if a surplus liquidity environment prevails in the banking system. This, in turn, could moderate the loan book growth for SIDBI as seen during the last one year.

Relatively concentrated exposure in indirect lending segment – SIDBI's lending is concentrated towards SCBs (82% as on September 30, 2021) followed by private sector entities excluding banks (9%) and NBFCs (~9%). With a high share of refinancing to banks, the concentration of the top 20 borrowers in the total exposure remained high at ~70% as on March 31, 2021 (~70% as on March 31, 2020). This is, however, mitigated by the limited credit risk in the refinance portfolio of banks.

Modest earnings profile mainly driven by fixed margins in refinance book – Given the cap on lending margins in the refinance business done through MSE funds and the increasing share of MSE refinance, the earnings profile, in terms of the RoA, remains modest. SIDBI's net interest margin (NIM) and gross interest spreads stood at 1.60% and 1.02%, respectively, in H1 FY2022 (1.94% and 1.47%, respectively, in FY2021). The refinancing book accounted for 92% of the net advances as on September 30, 2021. Accordingly, the earnings profile moderated with an RoA and RoE of 1.14% and 8.50%, respectively, in H1 FY2022 (1.26% and 11.27%, respectively, in FY2021). Going forward, any regulatory change, resulting in the narrowing of spreads, will remain a key monitorable for SIDBI's profitability.

Liquidity position: Superior

Refinance against RIDF deposits contributes to a significantly large percentage of the total advances (82% of total advances as on September 30, 2021). As these advances are covered against RIDF deposits with a similar maturity of 3 years, the overall Asset and Liability Management (ALM) profile remains well matched to a large extent. As a result, SIDBI had positive asset-liability gaps in the short as well as the long term as on September 30, 2021. It had undrawn bank lines of Rs. 9,900 crore and RIDF allocations to the tune of Rs. 21,093 crore as on September 30, 2021, which can be called on short notice and can be drawn to meet any shortfall/funding gaps in future.

Rating sensitivities

Positive factors – Not applicable

Negative factors – ICRA could assign a Negative outlook or downgrade the rating in case of a dilution in SIDBI's strategic role and importance to the GoI.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	ICRA Rating Methodology for Banks Impact of Parent or Group Support on Issuer's Credit Rating
Parent/Group Support	ICRA expects SIDBI to remain important to the GoI for supporting the growth of the MSME sector in India and expects the GoI to provide financial support, including MSE fund allocation and capital, if required
Consolidation/Standalone	For arriving at the rating, ICRA has considered the standalone financials of SIDBI. However, in line with its limited consolidation approach, ICRA has factored in the capital requirement of SIDBI's subsidiaries. In ICRA's view, the subsidiaries will remain self-sufficient in meeting their capital requirements in the near to medium term

About the company

Small Industries and Development Bank of India (SIDBI) is a financial institution, constituted under an Act of Parliament (SIDBI Act, 1989), for the promotion and development of the MSME sector in India.

SIDBI is jointly owned by SBI (largest shareholder with a stake of 16.73% as on September 30, 2021), the GoI (15.40%), LIC (14.25%) and other PSBs (the balance). ICRA notes that the GoI directly controls the operations of all the shareholders of SIDBI, which indirectly gives it total access over SIDBI's operations.

SIDBI's board of directors consists of –

- The Chairman & Managing Director appointed by the Central Government (for a term of 5 years)
- Two whole-time directors appointed by the Central Government
- Two directors who shall be officials of the Central Government
- Three directors to be nominated in the prescribed manner by the development bank, the PSBs, General Insurance Corporation of India (GIC), LIC and other institutions owned or controlled by the Central Government
- Three directors, including one from the officials of the state financial corporations, nominated by the Central Government from among persons having special knowledge of or professional experience in science, technology, economics, industry, banking, industrial cooperatives, law, industrial finance, investment, accountancy, marketing or any other matter
- Such number of directors, not exceeding four, elected in the prescribed manner by shareholders other than the development bank, the PSBs, GIC, LIC and other institutions owned or controlled by the Central Government

Key financial indicators (standalone)

	FY2020	FY2021	H1 FY2021^	H1 FY2022^
Net interest income	3,299	3,679	2,058	1,325
Profit after tax	2,315	2,398	1,535	945
Net advances	1,65,422	1,56,233	1,42,937	1,43,760
Total assets (Rs. lakh crore)	1.88	1.92	1.61	1.71
% NIM/ATA	1.92%	1.94%	2.50%	1.60%
% RoA	1.35%	1.26%	1.86%	1.14%
% RoE	12.18%	11.27%	14.95%	8.50%
% Tier I	26.62%	27.49%	29.02%	30.94%
% CRAR	26.62%	27.49%	29.02%	30.94%
% Gross NPA	0.63%	0.18%	0.47%	0.20%
% Net NPA	0.40%	0.12%	0.12%	0.13%
% PCR (excl write-offs)	36.6%	34.5%	74.4%	31.5%

Source: *SIDBI & ICRA Research; Amount in Rs. crore*
All ratios as per ICRA calculations
^Provisional

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Sr. No.	Name of Instrument	Current Rating (FY2022)				Chronology of Rating History for the Past 3 Years		
		Type	Rated Amount (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					Jan-10-2022	Jan-13-2021	Dec-31-2019	Dec-17-2018
1	Long-term Bonds Programme	Long Term	5,000.00	2,735.00*	**[ICRA]AAA (Stable)**	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)	[ICRA]AAA (Stable)

Source: *ICRA Research*

**Balance yet to be placed – bonds of Rs. 2,265.00 crore*

Complexity level of the rated instrument

Instrument	Complexity Indicator
Long-term Bonds	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instruments credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE556F08JK7	Long-term bonds	Apr-26-2019	7.95%	Apr-26-2022	1,365.00	[ICRA]AAA(Stable)
INE556F08JP6	Long-term bonds	Feb-27-2020	6.27%	Feb-27-2023	620.00	[ICRA]AAA(Stable)
INE556F08JQ4	Long-term bonds	Aug-18-2020	4.90%	Aug-18-2023	500.00	[ICRA]AAA(Stable)
INE556F08JR2	Long-term bonds	Dec-17-2020	4.58%	Dec-18-2023	250.00	[ICRA]AAA(Stable)
Unplaced	Long-term bonds	Unutilised	NA	NA	2,265.00	[ICRA]AAA(Stable)

Source: SIDBI

Annexure-2: List of entities considered for consolidated analysis

S. No.	Name of the Entity	Ownership	Consolidation Approach
1.	MUDRA Limited	100.0%	Limited Consolidation
2.	SIDBI Venture Capital Ltd (SVCL)	100.0%	Limited Consolidation
3.	SIDBI Trustee Company Ltd	100.0%	Limited Consolidation

Source: SIDBI and ICRA Research

Corrigendum

ROA% in H1FY2021 has been corrected to 1.86% in the key financial indicators table

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